No. 13126

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

CHRISTINE ALLEN,

Appellant,

vs.

RALPH MEYER, Trustee in Bankruptcy of the Estate of Joseph E. Allen, Bankrupt,

Appellee.

PETITION FOR REHEARING.

HARRY R. ROBERTS,
JESS G. SUTLIFF,
WM. HOWARD NICHOLAS,
634 South Spring Street,
Los Angeles 14, California,
Attorneys for Appellant.

Parker & Company, Law Printers, Los Angeles. Phone MA. 6-9171.

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Introduction.

In the oral argument of this case this Court through its Presiding Justice, indicated that it was not prepared to follow the District Court in its affirmance of the Order of the Referee under review in this appeal upon the grounds upon which that order was made. In the opinion of this Court, filed April 30, 1952, this Court has adhered to that position and appears to have conceded appellant's arguments that appellant's interest is in the assets of the business and not in net worth thereof and that the conversion of her community interest to a tenancy in common was not in violation of Section 3440 of the Civil Code. The Court now proceeds to hold adversely to appellant upon a theory of agency, a theory which has been

repudiated by both the District Court and the Referee. In applying a new and novel theory to the appeal, this Court has proceeded to decide the case without the benefit of comprehensive briefs on the point. We do not question the power of the Court to review the case upon a consideration of all of the questions which it sees as presented by the appeal. We do, however, consider the application of a new and novel theory to the appeal without the opportunity of counsel to be heard a dangerous expedient pregnant with possibility of error and the miscarriage of justice. Whenever an appellate court has made such a departure, however clear its authority may be to do so, a petition for a rehearing is singularly appropriate.

Assignment of Errors in the Opinion.

1. This Court has erred in its opinion by failing to consider the fact that all of the bankrupt's creditors had notice *as a matter of law* of the limitations imposed upon the bankrupt by the terms of the property settlement agreement by reason of the recording of the agreement in the County in which the business was located and in which the divorce proceedings were had.

2. This Court has erred in its opinion in that it has failed to consider that the property settlement agreement was recorded and the holding of this Court is contrary to Sections 165 and 166 of the Civil Code and the cases decided thereunder, to wit, *Carter v. McQuade* (1890), 83 Cal. 274 (23 Pac. 348), and *Shumway v. Leakey* (1885), 67 Cal. 458 (8 Pac. 12).

3. This Court has erred in its opinion in that it has construed the property settlement agreement as conferring upon the bankrupt express authority as appellant's agent to buy merchandise and generally to incur debts without limit upon the credit of appellant's interest in the assets of the business.

4. This Court has erred in its opinion in that it has construed the property settlement agreement as creating a broad general agency rather than a limited and restricted agency as existing between the bankrupt and appellant for the purposes of the conduct of the business.

5. This Court has erred in its opinion by failing to recognize that none of the creditors furnished merchandise or credit to the bankrupt on any basis except the bankrupt's individual credit.

6. This Court has erred in its opinion by failing to recognize that the prior adjudication that no partnership ever existed between the bankrupt and appellant necessarily implies that no general agency ever existed between the bankrupt and appellant.

7. This Court has erred in its opinion by holding that creditors who are charged by law with notice of the bankrupt's limited authority had superior rights to the bankrupt himself.

A. Under Sections 165 and 166 of the Civil Code, Each and Every Creditor of the Bankrupt Had Constructive Notice as a Matter of Law of Each and Every Term of the Property Settlement Agreement.

1. The Property Settlement Agreement Was Recorded in Inyo County and Was Entitled to Recordation Under the Law.

The property settlement agreement [Tr. p. 49] was, shortly after the entry of the Interlocutory Decree, recorded in the office of the Recorder of Inyo County [Tr. p. 32], the same being the County in which the drug store was located and in which the divorce proceedings were pending.

Section 165 of the Civil Code provides that either spouse may make an inventory of his or her separate personal property, and when signed by such spouses and acknowledged in the manner required by law for the acknowledgment of a grant of real property, the same may be recorded in the Office of the County Recorder in which the parties reside. The property settlement agreement fulfills the statutory requirements for an inventory in that it was signed by both parties and bears an acknowledgment [Tr. pp. 60-61]. It would appear that the property settlement was entitled to be recorded not only under the terms of Section 165 of the Civil Code, but also under Section 27322 of the Government Code which latter section enumerates the kinds of instruments entitled to recordation as including:

> "(j) Instruments describing or relating to the separate property of married women."

Moreover, since the property settlement agreement also provides for the disposition of two unimproved lots in the Town of Lone Pine, County of Inyo, it would also be entitled to recordation under the terms of Sections 1213 and 1215 of the Civil Code.

2. The Recording of an Inventory of the Separate Property Is Notice to the World of the Title of the Spouses and Is Prima Facie Evidence of Title as the Separate Property of the Spouses.

> "The filing of the inventory in the Recorder's Office is notice and prima facie evidence of the title of the party filing such inventory." (Civil Code, Sec. 166.)

Sections 165 and 166 of the Civil Code were intended to provide a wife with a means of protecting her separate property because of the inherent difficulty resulting from her relations as a wife (*Morgan v. Ball* (1899), 81 Cal. 93, 96, 22 Pac. 331). Section 27322 of the Government Code (formerly Sec. 4131 of the Political Code) is to be liberally construed with a view to effect its objects and to promote justice (*Beatty v. Hughes* (1943), 61 Cal. App. 2d 489, 143 P. 2d 110).

Not only in form would the property settlement agreement qualify as an inventory, but also in substances it had such a character, even though it was not so designated in the caption. The agreement provided for a complete disposition of the property owned by both the bankrupt and the appellant. By its terms the property transferred thereby was to be the separate property of the party receiving the same. The rights of appellant and the bankrupt as tenants in common in the assets of the drug store business were, of course, separate property.

3. **Where a Husband and Wife Separate and Enter Into a Property Settlement Agreement by the Terms of Which the Husband Transfers to the Wife Personal Property Without Any Intent to Hinder, Delay or Defraud Any of His Creditors, and the Wife Thereafter Records, Pursuant to Section 165 of the Civil Code, an Inventory of the Property Transferred to Her Under the Terms of the Property Settlement Agreement, It Has Been Held That the Transfer Is Valid Against the Husband's Creditors and Is Not Subject to Levy for His Debts.**

Carter v. McQuade (1890), 83 Cal. 274, 23 Pac. 348.

Accord:

Shumway v. Leakey (1885), 67 Cal. 457, 8 Pac. 12.

The husband's creditors are therefore within the class of persons conclusively charged with notice by the recording of an instrument describing or relating to the separate property of a married woman or providing an inventory of the same. It would appear from Section 166 of the Civil Code that a recorded inventory is notice to all the world of the title of a married woman to the property described therein as her separate property. Since this section was intended to operate so extensively, it should be liberally construed and is to be distinguished in its operation from other recording statutes which operate to impute notice only to a limited class, *e. g.*, subsequent purchasers and mortgagees (*Cf.* Civil Code, Sec. 1213).

4. **Constructive Notice and Actual Knowledge Are in the Contemplation of the Law Equivalent and the Bankrupt's Creditors Could Not Show That They in Fact Did Not Know of the Terms of the Property Settlement Agreement.**

The recording of an instrument gives constructive notice of its entire contents to all persons designated in the recording statute as bound by its terms (*Duncan v. Ledig* (1949), 90 Cal. App. 2d 7, 12, 202 P. 2d 107). The presumption of knowledge resulting from recordation of an instrument is conclusive and incontrovertible (*Anderson v. Willson* (1920), 48 Cal. App. 289, 293, 191 Pac. 1016; *Fair v. Stevenot* (1866), 29 Cal. 486, 488; 22 Cal. Jur. 616). Therefore, the creditors of the bankrupt herein could not by any competent evidence show that they did not have actual knowledge of the terms of the property settlement agreement, since under *Fair v. Stevenot, supra,* such evidence would be inadmissible.

There is no evidence in the record before this Court, or any finding to the effect, that the creditors of the bankrupt did not have actual notice of all of the terms of the property settlement agreement. The Trustee has introduced no evidence before the Referee that any creditor was any-wise actually prejudiced or lulled into a false sense of security by the terms of the property settlement agreement, as implemented by the divorce decree. If the Trustee had such evidence, the Trustee surely would have introduced it, and the Trustee was obligated under the law to present *all of his contentions*

to invalidate the claim of the appellant to the assets of the business and could not before the Referee litigate her title piecemeal. Since constructive notice is in law the equivalent actual notice, the creditors are in no position to claim special or preferential treatment.

B. The Property Settlement Agreement Is to Be Construed as a Whole and All of Its Provisions Are to Be Given Effect, and When so Construed, the Agency of the Bankrupt to Manage the Business Was a Limited and Special Agency to Operate the Drug Store in the Ordinary Course of Business Without, However, Any Authority to Incur Debts or Purchase Merchandise on the Credit of Appellant or Upon the Credit of Her Interest in the Drug Store.

1. The Property Settlement Agreement Specifically Denies to the Bankrupt Any Authority to Incur Any Debts or Liabilities Whatsoever on Behalf of the Appellant.

"First: That, except as hereinafter provided, each party hereto is hereby *released and absolved from any and all obligations and liabilities for the future acts and duties of the other, and that each of said parties hereby releases the other from any and all debts, liabilities and obligations of every kind and character incurred by the other from and after this date,* and from any and all claims and demands, including all claims of either party upon the other for support and maintenance as wife or husband or otherwise, it being understood that this instrument is intended to settle the rights of the parties hereto in all respects, except as hereinafter provided." [Tr. p. 50; italics added].

The clause in the above paragraph, "except as hereinafter provided," was a reservation to limit the generality of the release and to prevent the impairment of the executory obligations under the agreement. By the terms of the agreement, the husband was to pay to the wife $125.00 per month for child support, $225.00 per month to the wife herself, and the first $15,000.00 from the proceeds of the sale of the business, or in the event the business was not sold, to pay the wife $15,000.00 in installments as therein provided for her interest in the business, and in addition to set up a trust fund in the amount of $10,000.00 for the minor children.

2. The Management Clause Contained in the Property Settlement Agreement Constitutes a Mere Consent by Appellant to the Bankrupt's Operation of the Drug Store in the Ordinary Course of Business and for That Purpose the Bankrupt Was No More Than Appellant's Special Agent.

The management clause, *i. e.,* "The drug store shall remain under the active management and control of the husband," was inserted into the agreement for the obvious reason that the law requires any person to hold a license as a pharmacist to sell any drugs, nostrums, ointments or appliances for the treatment of disease, deformities or injuries (Bus. and Prof. Code, Sec. 4071). The obvious purpose and scope of the authority delegated to the bankrupt by the appellant by virtue of the management clause was to enable the bankrupt to sell the merchandise under his license as a registered pharmacist. There is no question that this clause enabled the bankrupt to pass good title to the merchandise purchased by the customers of the business. This Court reasons in its opinion from the premise that since the bankrupt could

pass good title to the merchandise, the bankrupt could subject appellant and her interest in the business to the liability to the payment of debts in the bankrupt's *purchase of merchandise.* This is a *non sequitur.* The purchase of merchandise and the sale of merchandise are entirely different matters and concern different classes of individuals whose rights rest upon different principles and who are separately treated in the property settlement agreement. We have already advanced the argument that the bankrupt's creditors were conclusively charged with notice as a matter of law that the bankrupt had no authority to incur any debts upon the credit of appellant or upon the credit or security of her interest in the business. The bankrupt's creditors sold merchandise to the bankrupt strictly on his individual credit. Charged with notice of his limited authority, his creditors could have dealt with him on no other basis, except, of course, on a cash basis.

3. The Test of the Rights of Creditors Is the Objective Test of What a Reasonable Man Would Believe Was the Authority of Bankrupt in Connection With the Business.

By reason of their constructive notice of the terms of the property settlement agreement, the bankrupt's creditors were no less bound by the limitations contained in the agreement than the bankrupt himself. The true test of the rights of the bankrupt's creditors is: Could a creditor as a reasonable man believe, knowing each and every term of the entire property settlement agreement, that the bankrupt had any authority in the purchase of merchandise or the incurring of debts in the operation of the business on behalf of the appellant or upon the strength of her interest in the business?

Certainly no competent lawyer could advise a creditor who submitted the property settlement agreement to him for an opinion, that his client would extend any credit to the bankrupt as the agent of appellant. His advice would be that without further authority from appellant, the creditor would have to look to the individual credit of the bankrupt or deal with him strictly on a cash basis.

Whatever vices the agreement may have from the standpoint of draftsmanship, these vices are its very strength. The agreement omits to provide for many contingencies which would normally arise. The novelty of the arrangement, the obvious omissions of protective provisions, the doubts which it engenders in any mind, are all factors which constitute a veritable "red flag" to creditors. There could be hardly a clearer warning to creditors than the specific provisions in the property settlement agreement denying to the bankrupt any authority to contract debts on behalf of appellant. These provisions are unambiguous and their understanding requires the services of no one specially trained in the law.

4. To Construe the Property Settlement Agreement as Creating a General Continuing Agency on the Part of the Bankrupt to Incur Debts and Liabilities Without Limitation on Behalf of Appellant in the Operation of the Drug Store, Is to Defeat One of the Primary and Principal Objects of the Property Settlement Agreement, Namely, the Final Settlement of Rights and Duties.

The property settlement agreement recites that it is the desire of both parties to accomplish a full and final adjustment of their property rights and claims [Tr. p. 49]. The very first covenant in the agreement releases and absolves each party from all obligations or the liabilities for the future acts and duties of the other, and

each of the parties thereby "releases the other from any and all debts, liabilities and obligations of every kind and character incurred by the other from and after this date," and concludes with the recitation that it is the purpose of the agreement to "settle the rights of the parties hereto in all respects, except as hereinafter provided" [Tr. p. 50]. The agreement further provides that all property acquired by either shall be the separate property of the party acquiring the same [par. "Second," Tr. p. 50], and the wife agrees to accept the provisions of the agreement in full satisfaction of her right to the community property and in full satisfaction of her right and support and maintenance [par. "Fifth," Tr. pp. 51-52].

If a general agency were created by the terms of the property settlement agreement for the bankrupt to incur debts without limit on behalf of the appellant, no finality in the settlement and adjustment of their rights would be accomplished. There can be no question that it was the intent of both the bankrupt and the appellant to deny to the bankrupt any authority to incur debts on behalf of the appellant or her interest in the business. Certainly this authority cannot be inferentially found in a mere isolated sentence when its existence is specifically denied by the agreement.

5. The Bankrupt Could Have Continued to Manage the Drug Store by Maintaining His Operation on a Cash Basis or Upon the Strength of His Own Individual Credit and This Was the Obvious Purpose and Plan Which the Parties Had in Mind When They Executed the Agreement.

There is no evidence before this Court that the creditors of the bankrupt extended any credit to him on any

basis other than his individual personal credit. Indeed, his creditors had no alternative except to insist upon cash payment since they were charged as a matter of law with notice of his special and limited authority so far as the rights of the appellant were concerned.

C. There Can Be No Actual or Ostensible Authority to Do an Act of Which the Third Person Has Actual or Constructive Notice the Agent Has No Authority to Perform.

1. **When a Third Person Has Actual or Constructive Notice of the Restrictions Placed Upon the Authority of the Agent, the Third Person Cannot Hold the Principal for the Agent's Acts in Contravention of His Authority.**

   Civil Code, Sec. 2318;

   Restatement of the Law of Agency, Secs. 166 and 167.

2. **Where Authority Is Given Partly in General and Partly in Specific Terms, the General Authority Gives No Higher Powers Than Those Specifically Mentioned.**

   Civil Code, Sec. 2321;

   Restatement of the Law of Agency, Sec. 37.

3. **Appellant Is Not Liable to the Bankrupt's Creditors on the Theory of Ostensible Agency Because There Is No Proof That Appellant Intentionally or Negligently Caused Any Creditor to Believe That the Bankrupt Had Any Authority to Bind Her by Any Contract.**

   Civil Code, Secs. 2317 and 2318.

4. **There Can Be No Ostensible Authority When the Third Person Has Actual or Constructive Notice of the Restrictions on the Agent's Authority.**

   Civil Code, Sec. 2318.

D. The Absence of a General Agency in the Bankrupt to Incur Debts in the Operation of the Business as the Agent of Appellant Is Implicit in the Adjudication That No Partnership Ever Existed Between Bankrupt and the Appellant in the Operation of the Business.

The opinion of this Court concedes for the purposes of the argument that appellant and the bankrupt acquired by virtue of the property settlement agreement, as implemented by the divorce decree, an interest in the physical assets as tenants in common. The opinion then proceeds to hold that a general agency existed in the scope of which the bankrupt was the agent of appellant for the purpose of incurring debts in the operation of the business. The difficulty with this reasoning is, among other things, that the Court has assumed one of the elements of the partnership, and deduces another element of partnership, and does not recognize that whenever common ownership in the assets of a business is coupled with a *general* agency between the co-owners in the conduct thereof, a partnership must as a matter of law exist between the co-owners. No other legal relationship is possible where common ownership and general agency between the owners coexist.

In the earlier bankruptcy proceeding the argument was made that by reason of the common ownership in the assets and an alleged general authority in the bankrupt to incur debts in the operation of the business, that the bankrupt and appellant were co-partners. This contention was rejected by the Referee. The Referee concluded

that no partnership whatsoever existed. This was an adjudication that neither an express partnership nor a partnership by estoppel was present. Unless a true estoppel exists by proof of either representation or acquiescence by the party to be charged and reliance thereon by a third person, no ostensible partnership can be proved. (*Hansen v. Burford* (1931), 212 Cal. 100, 297 Pac. 908; *Richlin v. Union Bank & Trust Company* (1925), 197 Cal. 296, 240 Pac. 782; *In re Brunson & Bunch,* 79 Fed. Supp. 833.)

That every partner is a general agent of his co-partner in the conduct of the partnership business is an elementary principal and has been incorporated in the Uniform Partnership Act.

Corporations Code, Sec. 15009, Subd. (1).

A partnership is defined as an association of two or more persons to carry on as co-owners, a business for profit (Corporations Code, Sec. 15006). The mere common property or part ownership does not itself establish a partnership whether such co-owners do, or do not, share any profits made by the use of the property (Corporations Code, Sec. 15007, Subd. (2)). The Uniform Partnership Act further provides that the sharing of gross returns does not of itself establish a partnership whether or not the persons sharing them have a common right or interest in any property from which the returns are derived (Corporations Code, Sec. 15007, Subd. (3)). The ultimate test of a partnership is

whether a community of interest exists between two or more persons in the conduct of the business for profit (*In re Brunson & Bunch,* 79 Fed. Supp. 833).

By concluding that a general agency existed between appellant and bankrupt in the conduct of the business, and by correctly conceding that the bankrupt and the appellant were co-owners of the assets of the business, this Court has ignored the fact that it now implicitly finds that a partnership existed between the appellant and the bankrupt. While the Court has not used the term "partnership," this conclusion is legally implicit and logically inescapable. To foreclose the contention ever being made that a general agency existed between appellant and the bankrupt is the very reason why counsel for the appellant insisted on findings by the Referee that it had earlier been adjudged that no partnership existed between the bankrupt and appellant in the conduct of the business. That order, of course, is an adjudication that no partnership, whether by consent or by estoppel, has ever existed between appellant and the bankrupt. That order and its necessary implications are as much binding on this Court as any other.

Conclusion.

The order of this Court will, unless set aside, result in a gross miscarriage of justice. The bankrupt has almost from the beginning breached his obligations under the terms of the property settlement agreement requiring appellant to institute a proceedings for its enforcement. This Court in its opinion has failed to consider many

relevant facts and has reached a conclusion not warranted by the record in this case or the law for the reasons hereinabove given. The creditors are entitled to no preferential treatment. Neither the bankrupt nor his creditors have rights superior to those of appellant. The opinion should be set aside and a rehearing granted.

Respectfully submitted,

HARRY R. ROBERTS,
JESS G. SUTLIFF,
WM. HOWARD NICHOLAS,
Attorneys for Appellant.

Certificate of Counsel.

I, Harry R. Roberts, counsel for Petitioner in the above entitled action, hereby certify that the foregoing petition for rehearing of this cause is presented in good faith and not for delay, and in my opinion is well founded in law and in fact, and proper to be filed herein.

HARRY R. ROBERTS,
Attorney for Petitioner.